

Message Text

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C O N F I D E N T I A L LIMA 4958

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TAGS: PINT, EGEN, PE, EINV

SUBJ: PRESSURES INCREASE ON GOP TO ANNOUNCE BASIC
ECONOMIC POLICY; PRIME MINISTER DECRIES
DEVALUATION RUMORS

REFS: A) LIMA 4920, B) LIMA 4722, C) LIMA 4658,
D) LIMA 4473

1. SUMMARY: IN INTERVIEW ON JUNE 18, PRIME MINISTER
MORALES BERMUDEZ WAS QUOTED BY CORREO AS STRONGLY DENYING
RUMORS OF IMPENDING DEVALUATION. PRIME MINISTER REITERATED
INFORMAL REMARKS OF PRESIDENT VELASCO ON JUNE 16 TO THE
EFFECT THAT THE GOP HAS WAGE/PRICE POLICIES UNDER INTENSIVE
REVIEW, ALTHOUGH HE SAID THAT NO DECISIONS HAVE YET BEEN TAKEN.
THE PRIME MINISTER'S REMARKS WERE MADE IN THE CONTEXT OF
A TIGHTENING CREDIT SQUEEZE BEING FELT WITH INCREASING
SEVERITY BY THE PRIVATE SECTOR, ITS EFFECTS INTENSIFIED
BY INCREASING INFLATION AND RUMORS OF DEVALUATION.
PRESSURES ARE GROWING ON THE GOP LEADERSHIP TO ANNOUNCE
ITS OVERALL WAGE/PRICE/SUBSIDY PACKAGE AS SOON AS POSSIBLE.
HOWEVER, EMBASSY UNDERSTANDS FROM GOP MILITARY SOURCE THAT
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AT REGULAR MEETING LAST TUESDAY, CABINET STILL FOUND ITSELF

UNABLE TO DECIDE PRECISELY WHAT MEASURES SHOULD BE TAKEN.
END SUMMARY.

2. DEVALUATION - MORNING CORREO OF JUNE 19 CARRIED BANNER HEADLINE "NO DEVALUATION," AND THEN QUOTED PRIME MINISTER MORALES BERMUDEZ IN EXCLUSIVE INTERVIEW THAT "...NEITHER THE ECONOMIC NOR SOCIAL SITUATIONS, WHICH ARE SOLID DESPITE THE INTERNATIONAL PRESSURES AT THIS TIME, PERMIT US TO CONSIDER SUCH A STEP." PRIME MINISTER ADDED THAT "SUCH A STEP AS DEVALUATION IS NOT INCLUDED IN THE ECONOMIC OR POLITICAL PLANS OF THE REVOLUTIONARY GOVERNMENT OF THE ARMED FORCES." CORREO COMMENTED THAT IT HAS BEEN BOMBARDED RECENTLY WITH HUNDREDS OF PHONE CALLS SEEKING INFORMATION ABOUT RUMORS OF A POSSIBLE DEVALUATION. CORREO CHARACTERIZED THE RUMORS AS "AN ARM OF THE COUNTER-REVOLUTION" BUT WENT ON TO NOTE THAT THESE RUMORS HAVE BEEN CIRCULATING IN THE BANKS, CAFES, TRADING HOUSES, MUTUAL INSURANCE COMPANIES AND COOPERATIVES, SO THAT THE NEWSPAPER FELT CONSTRAINED "TO GO TO THE HIGHEST LEVELS OF THE GOP" TO SCOTCH THEM.

3. PRIVATE SECTOR CREDIT CRUNCH - WITH THE RATE OF INFLATION NOW APPROXIMATEING 30 PERCENT ON AN ANNUAL BASIS DURING THE FIRST MONTHS OF THIS YEAR, DEMAND FOR PRIVATE SECTOR CREDIT HAS RISEN BECAUSE WHILE NOMINAL INTEREST RATES HAVE REMAINED UNCHANGED EFFECTIVE INTEREST RATES HAVE DECLINED. MOREOVER, BUSINESSMEN SEEK TO BORROW NOW IN THE EXPECTATION OF REPAYING IN EVEN MORE INFLATED SOLES. DURING ALL OF 1974, COMMERCIAL BANK LOANS TO THE PRIVATE SECTOR INCREASED BY ONLY S/.2.5 BILLION, BUT THROUGH FIRST FIVE AND ONE-HALF MONTHS OF THIS YEAR THE INCREASE IN LOANS TO THIS SECTOR HAS DOUBLED TO S/.5 BILLION. WHILE LOAN DEMAND HAS BEEN INCREASING, THE GOP HAS BEEN FOLLOWING A CAUTIOUS AND ONLY SLIGHTLY EXPANSIONARY CREDIT POLICY. IN ADDITION, CREDIT HAS BECOME TIGHTER BECAUSE OF SEASONAL FACTORS, INCLUDING REPAYMENT OF EXPORT CREDITS OBTAINED IN LATE 1974 AND EARLY 1975, AND CORPORATE TAX PAYMENTS WHICH FELL DUE IN APRIL. ALSO, THE RUMORS OF DEVALUATION HAVE CAUSED IMPORTERS AND INVESTORS TO SHY AWAY FROM HOLDING SOL BALANCES FOR LATER CONVERSION INTO DOLLARS TO REPAY INTERNATIONAL
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CREDITORS. ON THE CONTRARY, THEY ARE USING UP THEIR FOREIGN-EXCHANGE AUTHORIZATIONS AS RAPIDLY AS POSSIBLE, CONVERTING SOLES INTO FOREIGN EXCHANGE IN THE PROCESS.

4. WAGE/PRICE ELEMENT OF ECONOMIC PACKAGE MAY BE OVERTAKEN BY EVENTS - EMBASSY UNDERSTANDS FROM RELIABLE SOURCE THAT LAST TUESDAY'S CABINET MEETING FAILED TO RESOLVE DECISIONS ON WAGE/PRICE/SUBSIDY ISSUES WHICH HAVE BEEN

POSTPONED UNTIL NEXT MEETING. MEANWHILE, THE GOP HAS BEEN FACED WITH A SERIES OF STRIKES (SEE SEPTTEL) OR THREATS OF STRIKES IN SOCIAL SERVICES, INCLUDING SOCIAL SECURITY HOSPITALS, UNIVERSITIES AND ELECTRIC INDUSTRY, AND THE LABOR MINISTRY HAS BEEN MOVING TO MEET WORKER DEMANDS IN THE INTEREST OF LABOR PEACE. THUS, HESITATION TO ANNOUNCE A FINAL PACKAGE MAY BRING ABOUT A SITUATION IN WHICH INDIVIDUAL GROUPS OF WORKERS RECEIVE SETTLEMENTS IN EXCESS OF RATE OF INFLATION AND/OR PRODUCTIVITY GAINS, THEREBY UNDERMINING BASIC POLICY ON WAGES AND PRICES WHEN IT IS FINALLY DECIDED.

5. COMMENT: CONTRARY TO THE ASSURANCES BY PRIME MINISTER MORALES BERMUDEZ ON MAY 28 THAT THE GOP WOULD SOON CHANGE ITS POLICY OF MASSIVE GOVERNMENT SUBSIDIES AND DEVELOP A WAGE/PRICE POLICY (REF D) IT NOW APPEARS THAT THE CABINET IS HAVING REATER DIFFICULTY IN REACHING FINAL DECISIONS. ALL OF THIS INDICATES THAT THE PRESIDENT MAY BE TAKING A HAND--AT LEAST TO THE EXTENT OF RETAINING VETO POWER--IN THE DELIBERATIONS OVER ECONOMIC POLICY. IN FACT, IN A BRIEF EXCHANGE WITH JOURNALISTS ON JUNE 16, PRESIDENT VELASCO MADE A VEILED REFERENCE TO THE IMPENDING ECONOMIC DECISIONS BY NOTING THAT THE GOP HAS NUMEROUS POLICIES UNDER CONSIDERATION ("MEASURES OF GRAND IMPORTANCE FOR THE COUNTRY AND FOR THE GREAT MASSES OF THE POPULATION") BUT THAT HE COULD NOT SPEAK FURTHER IN DETAIL BECAUSE "WE HAVE TO ELABORATE THEM AND PUT THEM INTO EFFECT WITH CARE AND, ABOVE ALL, WITH MUCH CALM." WHETHER THIS DELAY IN MAKING DECISIONS REFLECTS A BASIC RADICAL-MODERATE SPLIT OVER THESE ISSUES IN THE CABINET, IN KEEPING WITH THE ANALYSIS IN REF A, OR MERELY DIFFICULTIES IN FINE-TUNING THE PACKAGE, OR BOTH, REMAINS TO BE SEEN.

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